

**MEMO# 28623**

December 30, 2014

## **SEC Issues Annual Staff Reports on Credit Rating Agencies**

[28623]

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TO:

FIXED-INCOME ADVISORY COMMITTEE No. 19-14  
MONEY MARKET FUNDS ADVISORY COMMITTEE No. 35-14  
MUNICIPAL SECURITIES ADVISORY COMMITTEE No. 30-14  
INVESTMENT ADVISER MEMBERS No. 33-14

RE:

SEC ISSUES ANNUAL STAFF REPORTS ON CREDIT RATING AGENCIES

On December 23, the Securities and Exchange Commission (the “SEC”) issued two separate annual staff reports on credit rating agencies that are registered as nationally recognized statistical rating organizations (“NRSROs”). The report titled “Annual Report on Nationally Recognized Statistical Rating Organizations” [\[1\]](#) (the “Congressional Report”), the latest in this line of annual reports submitted to Congress, is required by the Credit Rating Agency Reform Act of 2006 (the “Act”). [\[2\]](#) In accordance with the Act, the Congressional Report:

- Summarizes the NRSRO-related actions taken by the SEC over the past couple of years;
- States that, during the report period (i.e., from June 26, 2013 to June 25, 2014), the SEC did not receive any complete applications for initial registration as an NRSRO [\[3\]](#) or any complete applications from current NRSROs to register in additional ratings classes;
- Indicates that the three largest NRSROs (S&P, Moody’s, and Fitch) continue to maintain a large collective share of the market, but also recognizes that smaller NRSROs have made gains in certain market segments (e.g., U.S. commercial mortgage-backed securities);
- Notes positive developments in the marketplace with respect to transparency (e.g., certain NRSROs are issuing unsolicited commentaries on solicited ratings issued by other NRSROs, and some have issued unsolicited commentaries on asset classes); and
- Describes the conflicts inherent in the “issuer-pay” and “subscriber-pay” business

models and the relevant conflict-related rules and rule amendments adopted by the SEC in 2014 in accordance with the Dodd-Frank Wall Street Reform and Consumer Protection Act (the “Dodd-Frank Act”). [4]

The report titled “2014 Summary Report of Commission Staff’s Examinations of Each Nationally Recognized Statistical Rating Organization” [5] (the “Examination Report”), the latest in this line of annual reports, is required by Section 15E(p)(3)(C) of the Exchange Act. The Examination Report provides an overview of the SEC’s examination program; summarizes NRSROs’ responses to recommendations from previous reports and instances of remedial action; and summarizes the “essential findings” from the 2014 examinations of the NRSROs. [6] Particular points of emphasis for the 2014 examinations included the following:

- NRSROs’ written policies and procedures, controls, and documentation, if any, related to Information Technology (“IT”) and cybersecurity;
- NRSROs’ ratings activity or rating files related to government securities;
- Some NRSROs’ ratings-related activities and publications concerning certain new types of asset-backed securities; and
- Operations and rating activity by certain NRSROs’ foreign credit rating affiliates beyond that conducted in prior years.

The Examination Report concludes by noting that future examinations will cover the new and amended NRSRO rules that the SEC adopted in 2014.

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#### **endnotes**

[1] Available at [www.sec.gov/ocr/reportspubs/annual-reports/nrsroannrep1214.pdf](http://www.sec.gov/ocr/reportspubs/annual-reports/nrsroannrep1214.pdf).

[2] Section 6 of the Act requires that these Congressional reports identify applicants for registration as NRSROs under Section 15E of the Securities Exchange Act of 1934 (the “Exchange Act”); specify the number of and actions taken on such applications; and specify the views of the SEC on the state of competition, transparency, and conflicts of interest among NRSROs.

[3] Currently there are ten credit rating agencies registered as NRSROs.

[4] See Institute Memorandum No. 28368, dated September 10, 2014, for a description of these new rules and rule amendments.

[5] Available at [www.sec.gov/ocr/reportspubs/special-studies/nrsro-summary-report-2014.pdf](http://www.sec.gov/ocr/reportspubs/special-studies/nrsro-summary-report-2014.pdf).

[6] Section 15E(p)(3)(B) of the Exchange Act provides that each examination shall include a review of the following eight topic areas: (i) whether the NRSRO conducts business in accordance with its policies, procedures, and rating methodologies; (ii) the management of conflicts of interest by the NRSRO; (iii) the implementation of ethics policies by the NRSRO;

(iv) the internal supervisory controls of the NRSRO; (v) the governance of the NRSRO; (vi) the activities of the designated compliance officer of the NRSRO; (vii) the processing of complaints by the NRSRO; and (viii) the policies of the NRSRO governing the post-employment activities of its former personnel. The Examination Report's essential findings are organized by these eight topic areas.

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